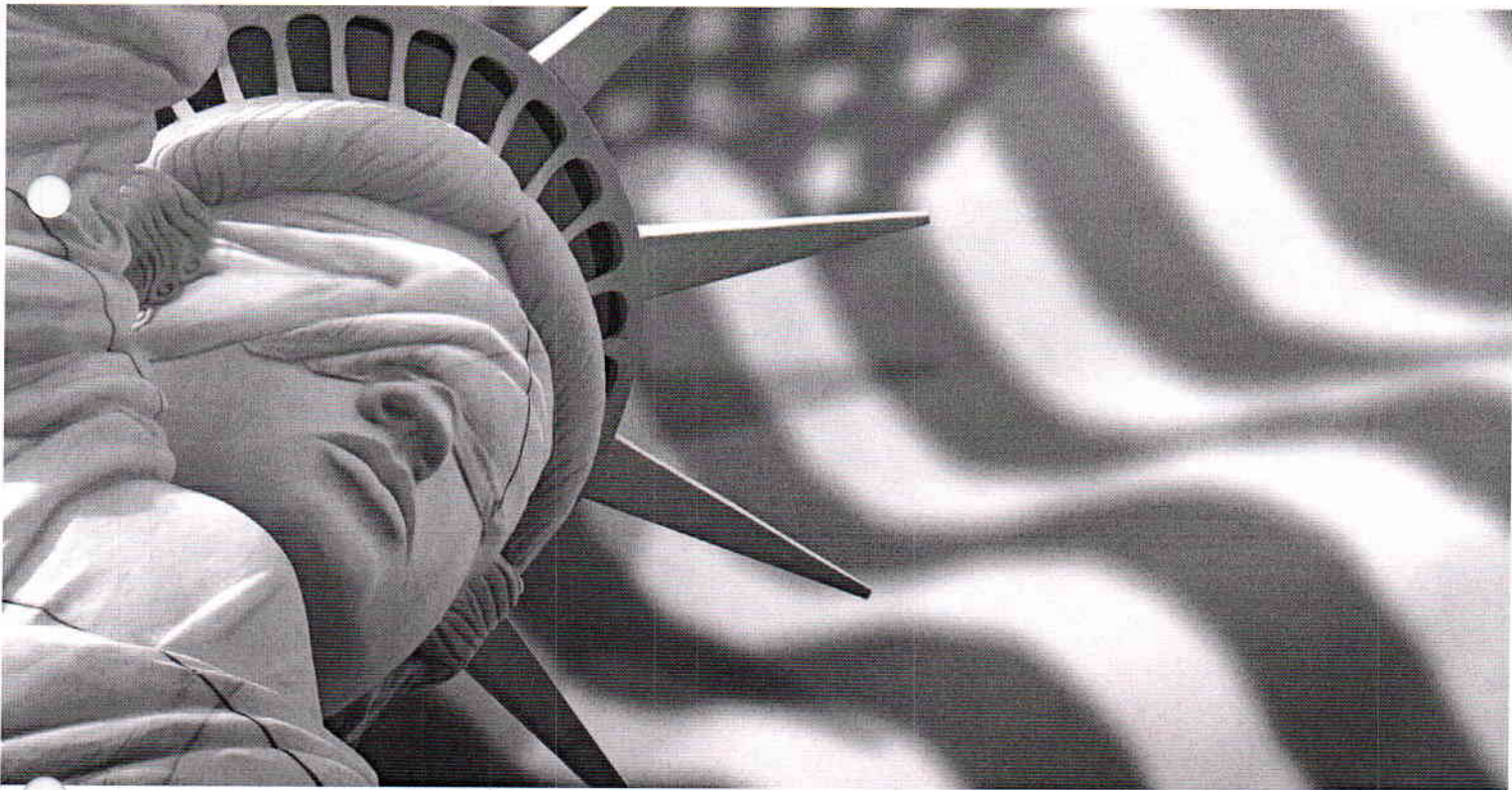


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The German Chamber Network 



Prof. Wolf M. Nietzer, MBA
Partner

Nietzer & Häusler
Wirtschaftskanzlei
Allee 40, 13. Stockwerk
4072 Heilbronn
T +49 (0)71 31 20 39 10
F +49 (0)71 31 20 39 12 0
info@unternehmensrecht.com
www.unternehmensrecht.com

NIETZER & HÄUSLER
Wirtschaftsanwälte - Attorneys at Law (USA) - Notar

Red Flag ALTER EGO / Piercing the Corporate Veil (Haftungsdurchgriff):

In principal, shareholder's liability in a corporation in the US is comparable to the one in Germany, this is, liability is limited to the paid in capital. But there are exceptions in the U.S. legal system as there are exceptions in German corporate law as well, commonly called Piercing the Corporate Veil. A Minnesota Court recently held that the following evidence established that the subsidiary was the parent company's alter ego:

(1) [The shareholder] is and has always been the sole shareholder; (2) [he] was the firm's sole incorporator; (3)[he], and no one else, gave loans to and borrowed money from the corporation; (4)[he] and his wife owned the building where the company was headquartered and received rental payments from the company; (5) the company purchased an automobile for [the shareholder's] business use which [he] also used for incidental personal business.

Furthermore, a West Virginia Court had stated possible prerequisites as follows:

1. commingling of funds and other assets of the corporation with those of the individual shareholders;
2. diversion of the corporation's funds or assets to non-corporate uses (to the personal uses of the corporation's shareholders);
3. failure to maintain the corporate formalities necessary for the issuance of or subscription to the corporation's stock, such as formal approval of the stock issue by the board of directors;
4. an individual shareholder representing to persons outside the corporation that he or she is personally liable for the debts or other obligations of the corporation;
5. failure to maintain corporate minutes or adequate corporate records;
6. identical equitable ownership in two entities;
7. identity of the directors and officers of two entities who are responsible for supervision and management (a partnership or sole proprietorship and a corporation owned and managed by the same parties);
8. failure to adequately capitalize a corporation for the reasonable risks of the corporate undertaking;
9. absence of separately held corporate assets;
10. use of a corporation as a mere shell or conduit to operate a single venture or some particular aspect of the business of an individual or another corporation;
11. sole ownership of all the stock by one individual or members of a single family;
12. use of the same office or business location by the corporation and its individual shareholders;
13. employment of the same employees or attorney by the corporation and its shareholder(s);



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14. concealment or misrepresentation of the identity of the ownership, management or financial interest in the corporation and concealment of personal business activities of the shareholders (sole shareholders do not reveal the association with a corporation, which makes loans to them without adequate security);
15. disregard of legal formalities and failure to maintain proper arm's length relationships among related entities;
16. use of a corporate entity as a conduit to procure services or merchandise to another person or entity;
17. diversion of corporate assets from the corporation by or to a stockholder or other person or entity to the detriment of creditors, or the manipulation of assets and liabilities between entities to concentrate the assets in one and the liabilities in another;
18. contracting by the corporation with another person with the intent to avoid the risk of nonperformance by use of the corporate entity; or the use of a corporation as a subterfuge to illegal transactions;
19. for formation and use of the corporation to assume the existing liabilities of another person or entity."

Thus, it is of utmost importance to German parent companies that management has a clear understanding on how to conduct business with its U.S. subsidiary so to avoid the application of the principle of Piercing the Corporate Veil at all times.



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